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C O N F I D E N T I A L SECTION 01 OF 02 KATHMANDU 000549

SIPDIS

STATE FOR SA/INS

E.O. 12958: DECL: 03/25/2013
TAGS: PREL EPET PGOV NP GON
SUBJECT: NEPAL: GOVERNMENT RAISES PETROL PRICES

Classified By: DCM Robert K. Boggs for reasons 1.5 (b,d)

¶1. (U) Summary: The Government of Nepal (GON) raised prices on all petroleum products to prevent further losses by state-owned Nepal Oil Corporation (NOC). The price increase should substantially reduce the corporation's monthly losses, but will not produce a profit. Prior to the increase, rumors and legitimate concerns about the future solvency of the NOC sparked fuel hoarding by industry and consumers, prompting the GON to take several measures to prevent a shortage. Popular perception that the Gulf War would limit supply contributed to the problem. End summary.

FUEL PRICES NOW ON PAR WITH INDIA

¶2. (SBU) On March 26, at the recommendation of the Nepal Oil Corporation (NOC), the Government of Nepal (GON) announced substantial price increases on all petroleum products, to bring them into line with fuel prices across the border in India. The government also has reintroduced a two-tiered pricing and rationing system for kerosene, the fuel most commonly used by domestic consumers. Under the new system, "middle and lower class consumers" will pay 5 Nepali rupees (6 cents) less per liter than industrial and "upper class" purchasers and will receive rationing coupons allowing them to purchase up to 10 liters of kerosene per month. However, no criteria have been established yet for "middle and lower class" designation, and a source at the Ministry of Industry, Commerce and Supply told Political FSN that, in reality, one coupon would likely be provided to every family that requests one, regardless of economic status.

¶3. (U) Prior to the price hike, fuel prices in India were substantially higher than those in Nepal. In towns along the border, the Indian price per liter for kerosene was almost 11 Nepali rupees (14 cents) higher than in Nepal. The price of a liter of diesel was approximately 10 Nrs (13 cents) higher, and the cost of a liter of petrol was approximately 4.5 rupees (5 cents) higher. Since Nepal imports fuel exclusively from India, the disparity in prices caused the NOC to post monthly losses running into the hundreds of millions of rupees, and the state-owned corporation has been seeking a price increase for the last eight months.

RUMORS ABOUND; SO DO REAL PROBLEMS

¶4. (U) Media reports stating that the NOC was in dire straits convinced companies that a severe price hike was in the offing. As a result, over the past few weeks industrial consumers purchased excessive amounts of fuel, despite already holding large stockpiles. Domestic consumers, worried by the same reports as well as by media-fed rumors that the war in the Gulf will further restrict supply, lined up outside fuel stations to purchase far more than usual. In addition, large quantities of cheaper fuel were flowing back across the border for resale at Indian prices. Consumer hoarding and the artificial demand from India were depleting the already small petroleum reserves, reported to be about 17 days worth of fuel, held by the NOC.

¶5. (U) To try to check "panic buying" among consumers, on March 22 the GON decided to place restrictions on the number of vehicles allowed on the roads. Cars with even-numbered license plates were allowed to travel on even-numbered days, and odd-numbered vehicles on odd-numbered days. However, on March 26, the Supreme Court placed a temporary stay on the enforcement of the restrictions, pending a final verdict on the measure's legality.

HALF A SOLUTION IS BETTER THAN NONE

¶6. (C) Public concerns about the solvency of NOC were well-founded. On March 24, PolFSN spoke to Bijendra Singh (protect), Chief of Distribution for NOC, about the unfolding events. According to Singh, the NOC is almost completely out of funds, and is "not in a position to settle its bill with the Indian Oil Corporation." The next payment, for fuel purchases in February and March, is due on April 15. In the event of non-payment, the IOC has already indicated that it will cut off supply to Nepal. According to the acting chief

of the NOC, contacted by PolFSN on March 26, by the end of March, NOC will owe a total of 930 million Indian rupees (IRs) (19.5 million USD) to the IOC, and will make a partial payment of 450 million IRs (9.5 million USD). By April 15, the amount due will be up to 1.8 billion IRs (37.8 million USD), of which the NOC plans to pay 800 million IRs (16.8 million USD). The acting chief could not explain how the NOC plans to pay the remaining amount.

¶7. (C) Following the price hike, Rudra Bahadur Khadka, Managing Director of the NOC, told reporters that the increase has addressed the root of the problem, as the selling price is now equal to the import price. However, the acting Chief of the NOC told PolFSN that the recent increase in price will simply reduce the corporation's losses, and that the corporation would be able to clear only partially its balance with the IOC. According to the acting chief, the Nepali corporation had been losing approximately 750-800 million Nrs (9.6 - 10.3 million USD) per month; monthly losses will now be 100-120 million Nrs (1.3 - 1.5 million USD).

COMMENT

¶8. (C) The price increase for petrol products is likely to stretch the budgets of Nepal's middle and lower classes, but the measure was a necessary evil. NOC's mounting losses created an artificial situation in which kerosene cost less than mineral water. The country's continued fuel supply was at risk and its limited current supply, purchased at a loss, was flowing back across the border. While the proposed two-tiered pricing system and rationing cards for kerosene may be an artful political dodge, it would be better for Nepal to bite the bullet now and raise prices across the board. If the two-tier system is implemented, it will simply reduce the urgently needed revenue that the price hike is intended to generate, and prolong the NOC's inability to meet its financial obligations. Crises like this week's will continue to arise as long as government subsidies continue to co-exist with a lengthy, porous international border. Post will continue to monitor the situation for potential political backlash, either tied to the war in the Gulf or directed solely at domestic actors.
MALINOWSKI